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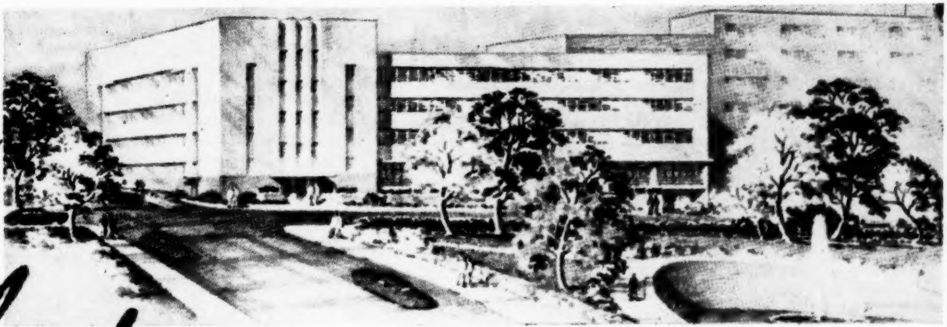

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THE DEMAND FOR HOUSING

by
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An issue which is currently very controversial is that of housing. With the government invading the field to a considerable extent and with regulations on building, there is a hue and cry on the matter. Many charges and counter-charges have been made and many statements have been lightly tossed about.

One frequently sees the statement that the demand for housing will do this or that as a result of governmental action, or a statement that the demand for housing will increase if the government will remove some of its current restrictions. Many of the statements appearing in the press are based on little or no knowledge. A search of the literature in the field will reveal that relatively little is known about the demand for housing, and, while many statements are made as to what will happen, most authors avoid any theoretical discussion. Consequently, it would be a good idea to look a little into the subject.

Real Estate Market a Local Disorganized One

The real estate market consists of a number of markets widely scattered geographically and partially isolated from each other. Therefore, there is really no national market for the purchase and sale of real estate in the sense that exists in securities and most commodities. One market may be enjoying a real estate boom while another is in a real estate depression, as demand cannot be shifted from a market with a small supply to one having a surplus of houses, as is the case in the market for wheat. Even within a single city, separate markets exist for houses in different neighborhoods and for houses of different sizes and prices. Therefore, the area within which the price-making forces operate is ordinarily very small; and if there could be such a thing as a national market, it is certainly highly disorganized. In these small markets there will be some tendency to overlap and in that respect one market may influence another; but the greater the distance between the two markets, the less the influence of one upon the other.

The Commodity Housing

When one thinks of housing as a commodity, he will normally think of the physical object—the house. While this is the physical unit which is bought and sold, the commodity itself actually consists of the services one obtains from that physical piece of property. The services include not only shelter from the elements, but also a number of important psychological elements such as prestige, pride in ownership, and others. So it will be well to realize that while it is the physical unit which is bought and sold, it is the services which in fact constitute the commodity.

Demand for Housing

Demand is commonly defined as "A schedule of all the various amounts that buyers stand ready to buy at a corresponding schedule of prices, at any given time and place."[1] In any discussion of the demand for housing, it should be borne in mind that the housing unit is desired only as a means to an end and that the buyers are actually demanding the services of the housing unit. Actually what the people are after in the housing market is services. The services of residential housing and improvements are bought and sold

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[1]John Ise, *Economics* (New York: Harper and Brothers Publishers, 1950), p. 166.

and exchanged between buyers who try to buy at the lowest price possible and sellers who try to obtain the highest possible prices. Housing services may mean those values either economic, social, or psychic, which are provided by a certain dwelling over a given period of time.

Variable Role of the Consumer

The consumer may occupy several different relationships to housing. He may be a tenant, owner who lives in his house, or owner who lives in a portion of his home and leases the remainder to others to secure returns on his investment in the form of rent. The same person may occupy several of these relationships to housing simultaneously or move from one to another. A shift from tenant to owner status may be of vital importance in studying the elasticity of demand for housing.

Some Important Factors Affecting The Demand For Housing

Terms and Availability of Credit

Most buyers of houses today enter the market with some money of their own, but have to rely quite heavily on some financial institutions. Therefore, the amount which they will be able to pay for their home is at least in part dependent on the amount of credit available to them. Under circumstances such as these, it is possible to have the demand for housing fluctuating not because of changing desires on the part of the prospective purchasers, but because of fluctuations in the amount of credit made available.[2] Demand consists not only of desire alone, but of desire coupled with the ability to buy; and that ability is in large measure dependent upon the lending institutions.

The standards of the mortgage lenders change from time to time. Unfortunately the changing standards tend to accentuate differences in income rather than equalize them. For example, lending institutions were much more liberal with their funds in prosperity than in depression.

The lenders also vary the amount they will lend according to the income of the borrower and according to the appraisal of the property under consideration. This recognition of the borrower's income tends to exaggerate the effect of changes in income on the real estate market and hence upon the price of housing.

The lending institutions also have to take into consideration the amount of funds available for financing real estate. They have other types of investments competing for the same money. Most of this is determined by conditions and events entirely outside the real estate market. This tends to some extent to tie the demand for housing to the investment market.

The terms of credit affect the demand for housing as well as availability of credit. A variation in the terms for which loans will be granted and the amount of the monthly payment to be made will also affect demand. For example, a decrease in the term for which a given loan will be made will increase the amount of monthly payments. An increase in the amount of monthly payments should probably cause the price which the buyer would be willing to pay to move in a downward direction.

Savings

As was mentioned before, a major portion of the funds used in the purchase of houses comes from lending institutions in the form of mortgage loans. About one-fifth of the amount spent in the purchase of homes in 1946 and 1947 came out of savings in the form of liquid assets. The increase in effective demand, therefore, reflected in part the wartime growth of savings, which in turn was a result of rapid increases in income or buying power not used during the war period. Holdings of liquid assets—currency, demand deposits, time deposits, savings and loan shares, and U. S. Government securities—by individuals increased from about $50,000,000,000 prewar to $150,000,000,000 at the close of the war.[3] These savings were also more widely distributed than ever before in our history. This gave rise to a situation in which more people than ever before in the history of the nation had available the amount necessary for the down payment on a home. Hence, the number of buyers in the market had been increased at a time in which the available supply of housing had increased by only a very small amount.

Influence of Government

The real estate market is greatly affected by governmental action. One reason for this is the fact that real estate is not actually a commodity so much as it is merely a bundle of rights created by government and law.[4] Such things as building codes, zoning ordinances and other limitations to use will exert a profound effect upon demand. Certainly any change in these factors will cause some change in demand, although it might not be possible to predict with accuracy just what that change will be. One would suspect that a tightening of building codes would lead to a decline in demand as some purchasers might drop out of the market entirely. If the purchasers did not drop out entirely, it might cause a shift in demand such that buyers are not now willing or able to pay as high a price as before for a home.

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[2]Donald S. Thompson (Vice-President Federal Reserve Bank of Cleveland), *Land Economics* (February, 1949), p. 111. Approximately half of the purchasing power for housing in 1946 and 1947 was obtained by borrowing. Mortgage loans increased more rapidly than in any comparable period for which we have reliable estimates. At a time when buying power was already excessive in terms of supply of housing, that buying power was increased by expansion and liberalization of credit facilities. Guarantees were provided, a secondary market created, maturities were extended, interest rates were lowered, loan ratios increased, and appraisals "liberalized". The result permitted the capitalization into higher real estate values of incomes which were in themselves also increasing.

[3]Ibid., p. 110.

[4]Edward E. Edwards, "Real Estate Economics: A Return to Fundamentals," *The Appraisal Journal*, (April, 1949).

In an effort to stimulate employment to some extent and also in an effort to see many income groups more adequately housed, the federal government has undertaken various programs aimed at making funds available more readily to borrowers in certain classes. This means that many buyers, who were formerly confined strictly to the rental market, have a chance to enter the market for owner-occupied housing. This, of course, tends to increase the quantity of housing demanded, especially housing in the lower price range.

Besides entering directly into the loan field, the federal government exercises a considerable measure of supervision over the policies of the various financial lending institution of the country. The federal government can help to tighten or ease the availability of funds and in this manner can affect the demand for housing.

Concluding Statements

There are a number of factors affecting the demand for housing. Probably the two most important are actions of the government and the terms and availability of credit. This is an important distinction between the demand for housing and the demand for many other commodities, such as wheat.

It would seem that there is a considerable degree of elasticity in the demand for housing. This is true both from the standpoint of income and price as well as substitution of rental housing for owner-occupied housing.

It is apparent that there is a need for much further research in the field, especially of the statistical variety. Statistical data to serve as a test are difficult to obtain, but if available they would prove of great value in testing conclusions of analysis. Mr. D. V. Cannon wrote a very interesting article in *Land Economics* pointing up the great need for further research and he apparently felt that much of it would have to be done on the local level.[5]

[5]Douglas V. Cannon, "Cities Meet the Need for Housing Research," *Land Economics*, (August, 1950), pp. 284-294.

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